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C O N F I D E N T I A L SECTION 01 OF 02 JERUSALEM 000401

SIPDIS

SIPDIS

NEA FOR A/S WELCH; NEA/IPA FOR WILLIAMS/SHAMPAINE/BELGRADE;
NSC FOR ABRAMS/DORAN/WATERS; TREASURY FOR
NUGENT/HIRSON/LOEFFLER/HARRIS;

E.O. 12958: DECL: 02/23/2016
TAGS: EPET ENRG EINV PREL KWBG IS
SUBJECT: UPDATE ON COMMERCIAL DEVELOPMENT OF OFFSHORE GAZA
NATURAL GAS FIELD

REF: A. 2006 CAIRO 3664

¶B. 2005 JERUSALEM 4999
¶C. 2005 JERUSALEM 1657

Classified By: Consul General Jake Walles, Reasons 1.4 (b) and (d)

¶1. (C) Summary: According to the Economic Advisor to the PA Presidency, British Gas (BG) continues to negotiate with the Israeli government on the sale of natural gas from the offshore Gaza natural gas fields. British Gas is the operator of the consortium licensed to commercially develop the fields. The consortium partners (BG, the Consolidated Contractors Company (CCC) and the Palestinian Investment Fund (PIF)) have also agreed that the main onshore delivery terminal should be in Ashdod, though they are still negotiating how to deliver a portion of the gas to Gaza, mostly to power the Gaza Power Plant. Since the PA will likely earn between USD 50-100 million per year in taxes and royalties, we understand BG is working with the PA Presidency on a transparent and auditable mechanism for the transfer of these funds that will not run afoul of U.S. and European regulatory restrictions regarding transactions with the PA. End summary.

BG negotiating sale of gas to
Israel, on behalf of consortium

¶2. (C) PA Presidency Economic Advisor and Managing Director of the Palestine Investment Fund (PIF) Mohammed Mustafa told the Consul General last month that negotiations are progressing between British Gas (BG) and the Israeli government on the sale of natural gas from the offshore Gaza gas fields. Mustafa said that since Yossi Bahar was named to lead negotiations on the Israeli side, BG has told the PIF that there has been a positive change in the GOI's approach to the negotiations. If the deal moves forward, BG, as the operator of the consortium, would sign the necessary agreements with the GOI, Mustafa said.

¶3. (C) Background: The Palestinian Authority granted BG an exploration license in 2000 covering the entire marine area offshore the Gaza Strip. Within this area, BG identified two natural gas fields: the Gaza Marine field and the Noa South field which continues into Israeli offshore waters (the Israeli portion of which is already under commercial development). While the original concession deal was structured with BG holding 90 percent and CCC 10 percent. CCC can chose to exercise its development option, thereby increasing its share to 40 percent and decreasing BG's to 60 percent. There was also an understanding that the PA could

exercise a 10 percent investment stake if it raised the necessary development funds (total development costs are estimated at USD 700 million). Salam Fayyad, when he was PA Finance Minister and head of the PIF, began negotiations to raise the PA's investment stake to 20 percent by having the other two parties agree to reduce each of their own interests by 5 percent. Negotiations continues on this, according to PIF staff. End background.

Consortium still negotiating
delivery of portion of gas to Gaza

¶4. (C) Mustafa told the Consul General that the consortium parties, including the PIF, have agreed that the main delivery terminal will be in Ashdod since the vast majority of the gas will be sold to Israel. Mustafa said that discussions continue on how to bring some of the gas to Gaza for the Gaza Power Plant. (Note: The PA is responsible for purchasing the fuel for the privately-operated Gaza Power plant. Switching the plant from diesel to natural gas will lower the PA's costs by about 50 percent. CCC owns more than one-third of the Gaza Power Plant, through shares held by a U.S. subsidiary Morganti Development LLC and directly through CCC-owned shares. End note.) Mustafa separately noted that he is working on interim natural gas provision arrangements for the Gaza Power Plant, likely from Egypt, since commercial production of the Gaza offshore fields is not likely to start before 2011.

PA to reap taxes and royalties
totaling USD 50-100 M

¶5. (C) When the field becomes commercially operational, the

PA will likely earn between USD 50-100 million per year in taxes and royalties from the offshore gas field license. Give the financial restrictions regarding transactions with the PA, we understand that BG is working with the PA Presidency to establish a transparent and auditable mechanism for the transfer of these funds to the PA. (Note: PIF staff were not prepared to share with ConGen EconChief any details of a possible mechanism, citing ongoing negotiations with BG. End note.)
WALLES